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NOT TO BE PUBLISHED

Commonwealth of Kentucky

Court of Appeals

NO. 2015-CA-000658-MR

PAUL V. BROOKS AND
DEMOISEY LAW OFFICE, PLLC — APPELLANTS

v.

APPEAL FROM FAYETTE CIRCUIT COURT
HONORABLE THOMAS L. CLARK, JUDGE
ACTION NO. 12-CI-001497

J.P. MORGAN CHASE BANK, N.A. — APPELLEE

OPINION
AFFIRMING

** ** ** ** **

BEFORE: MAZE, STUMBO, AND TAYLOR, JUDGES.

MAZE, JUDGE: Appellants, Paul Brooks and the DeMoisey Law Office (hereinafter, "DeMoisey"), appeal from an order of the Fayette Circuit Court dismissing their crossclaims and counterclaims against J.P. Morgan Chase Bank (hereinafter "Chase") and overruling its motion for summary judgment. Brooks

and DeMoisey contend that the trial court erred when it held that Chase held an "equitable mortgage" and that Chase's mortgage enjoyed priority over a lien DeMoisey held on the same property. We observe no error in the trial court's judgment. Therefore, we affirm.

Background

On February 27, 2004, Brooks signed a promissory note ("the Note") on a loan from Sunset Mortgage for $379,200.00. The Note was immediately assigned, by attached allonge, to Washington Mutual Bank, B.A. (hereinafter "WAMU"). Brooks subsequently made payments to WAMU on this note.

The same day, Brooks signed an instrument titled "Mortgage," a "certified true" copy of which appears in the record before this Court. This document listed the mortgagee as the Mortgage Electronic Registration System, Inc. (MERS) and the "borrower" as Brooks and his then-wife, Denise. However, only Brooks signed the Mortgage and the Note. While Brooks's signature was notarized, the preparer of the document is unidentified, and the document lacked a "scrivener's statement." Additionally, though the Mortgage stated that a legal description of the subject property was attached as "Exhibit A," the document identified as "Exhibit A", entitled "Legal Description," was blank. Neither WAMU nor any party or subsequent holder of the Note recorded the Mortgage, and the original document was apparently lost.

In September 2008, WAMU was placed in receivership, with the Federal Deposit Insurance Corporation (FDIC) serving as receiver. By agreement,

Chase acquired "all of the assets (real, personal and mixed, wherever located and however acquired)" formerly held by WAMU. Upon review of the mortgages it acquired under this agreement, Chase apparently discovered the missing and unrecorded mortgage document on the Brooks property, and it sought legal recourse in the form of the instant action.

On March 28, 2012, Chase filed suit in Fayette Circuit Court seeking leave to file a photocopy of the Mortgage with the Fayette County Clerk. Chase also sought adjudication of its lien's priority over others filed against the same property. After conducting a title search to identify such claims, Chase provided notice of its suit to another law firm, Brooks, Morris, and Morris, PSC, and State Street Bank. Chase also filed a *lis pendens* notice on the property two days after filing suit.

On April 23, 2012, almost a month after Chase filed its suit, DeMoisey recorded a document entitled "Mortgage" with the Fayette County Clerk. This document, dated seven days prior, claimed an interest in the Brooks property secured in the amount of $53,280.00 as apparent consideration for legal services DeMoisey performed for Brooks in unrelated legal matters. DeMoisey subsequently intervened in the present action to assert its interest in the Brooks property and the superiority of its lien over that of Chase.

After both parties filed several motions, including Chase's motions to dismiss Brooks's and DeMoisey's crossclaims and counterclaims, the trial court entered an order on April 7, 2015, and an amended order on April 16, 2015,

granting Chase's motions and overruling Brooks's and DeMoisey's motion for summary judgment. This appeal follows.

Standard of Review

The trial court heard this case without the benefit of a jury. Accordingly, we will not disturb its findings of fact absent clear error, and we must give due regard to the trial court's supreme ability to hear the evidence and judge the credibility of witnesses. CR[1] 52.01; *see also Moore v. Asente*, 110 S.W.3d 336, 354-55 (Ky. 2003). A finding is clearly erroneous only if it lacks the support of substantial evidence in the record. *Moore* at 355 (citation omitted). Additionally, we review *de novo* the trial court's application of the law to the facts. *See A & A Mech., Inc. v. Thermal Equip. Sales, Inc*., 998 S.W.2d 505, 509 (Ky. App. 1999).

Analysis

On appeal, DeMoisey and Chase each contend that the other lacked a valid lien, and therefore lacked standing to challenge the other's interest in the Brooks property. We must first resolve these questions of standing before proceeding to the more substantive issues DeMoisey raises on appeal.

I. Standing and the Validity of Both Liens Under Kentucky Law

To have standing in a given case, a party's interest "must be of a direct and immediate character so that the intervener will either gain or lose by the direct legal operation of the judgment." *Stuart v. Richardson*, 407 S.W.2d 716, 717 (Ky. App. 1966). In other words, a party must possess "some right to protect

[1] Kentucky Rules of Civil Procedure.

which is not being protected." *Id*. In the context of this case, each party claims that its interest arises from a lien against the Brooks property memorialized by a mortgage document. Therefore, to determine standing, we must first look to whether these, and other, documents comply with Kentucky law regarding the validity of liens.

A. DeMoisey's Lien

After originally raising the issue in response to DeMoisey's Motion to Compel, Chase challenges DeMoisey's lien, arguing that DeMoisey lacks standing and that its appeal must be dismissed. Chase contends that, though it was titled "Mortgage," DeMoisey's lien was actually an attorney's lien governed under KRS 376.460. On this basis, Chase argues that DeMoisey's lien could not attach to, or affect, the Brooks property, depriving DeMoisey of standing in the present action. We disagree.

KRS 376.460 provides for an attorney's interest in sums recovered to the extent he should be paid for his services. However, such a lien is not the only method by which an attorney may collect payment or protect his right to do so. A mortgage lien on real property is another, albeit less conventional, method; and it is the method Brooks and DeMoisey chose under the circumstances of the litigation which preceded the instant case. We cannot agree with Chase that this removes DeMoisey's lien from the realm of mortgage liens governed under KRS Chapter 382, nor can we agree that it automatically invalidates DeMoisey's lien on the Brooks property. The trial court correctly proceeded past this issue.

B. Chase's Lien

DeMoisey challenges the validity of Chase's lien on the basis that the Mortgage did not comply with several requirements in Kentucky law for a valid lien. As a result, DeMoisey contends that Chase neither had standing nor an equitable mortgage for the Brooks property, contrary to the trial court's conclusion.

To possess an equitable mortgage under Kentucky law, there must be a transfer of a promissory note secured by a mortgage. *Drinkard v. George*, 36 S.W.2d 56 (Ky. 1930). DeMoisey contends that, due to several defects in the Mortgage, there was no such transfer and hence, no equitable mortgage. We disagree.

As DeMoisey points out, Kentucky law concerning transfers of real property require documents memorializing those transfers to contain items such as a scrivener's statement, a legal description of the property, and a spouse's signature before they can be recorded. *See* KRS 382.335. Chase also points to the fact that MERS, and not Sunset Mortgage, is listed as the "mortgagee" on the Mortgage. However, none of these facts is dispositive of, or otherwise affects, the efficacy of the Note Chase now holds nor the fact that Chase holds an equitable mortgage in the Brooks property.

While these defects might prevent the Fayette County Clerk from receiving and recording the Mortgage under KRS 382.335, they do not act to invalidate the Mortgage itself or Chase's resulting equitable mortgage in the Brooks property. First, MERS's involvement in the transaction is commonplace

practice in such transfers, and was explained in a relatively recent case before the Sixth Circuit Court of Appeals:

> When a home is purchased, the lender obtains from the borrower a promissory note and a mortgage instrument naming MERS as the mortgagee (as nominee for the lender and its successors and assigns). In the mortgage, the borrower assigns his right, title, and interest in the property to MERS, and the mortgage instrument is then recorded in the local land records with MERS as the named mortgagee. When the promissory note is sold (and possibly re-sold) in the secondary mortgage market, the MERS database tracks that transfer. As long as the parties involved in the sale are MERS members [as are most large financial institutions], MERS remains the mortgagee of record (thereby avoiding recording and other transfer fees that are otherwise associated with the sale) and continues to act as an agent for the new owner of the promissory note.

Higgins v. BAC Home Loans Servicing, LP, 793 F.3d 688, 689 (6th Cir. 2015), *quoting Christian Cty. Clerk ex rel. Kem v. Mortg. Elec. Registration Sys., Inc.*, 515 Fed.Appx. 451, 452 (6th Cir. 2013). Though it may be controversial, this practice is permitted under prevailing Kentucky law; and it does not affect the validity of the liens involved. DeMoisey's reliance upon MERS's involvement as a means of invalidating Chase's interest in the Brooks property is misplaced.

Similarly, the failure of Chase and its predecessors to record the Mortgage did not invalidate Chase's claim. It is well established in Kentucky law that failure of an assignee to record a mortgage or mortgage assignment does not affect the validity or perfection of a mortgage lien. *See, e.g., Stevenson v. Bank of Am.*, 359 S.W.3d 466, 470 (Ky. App. 2012) and KRS 382.360(6) ("Failure of an

assignee to record a mortgage assignment shall not affect the validity or perfection, or invalidity or lack of perfection, of a mortgage lien under applicable law.). A mortgage document and its proper assignment to another party is not what transfers enforcement rights on a promissory note to a subsequent holder. *Stevenson* at 470. Mere possession of the original note is sufficient. *Id*. Therefore, that Chase possessed the Note, as long as the Note was properly assigned to it and its predecessors in interest, is sufficient to transfer its interest and its lien. *Stevenson* at 470; *see also Drinkard v. George*, 36 S.W.2d 56 (Ky. 1930).

Despite DeMoisey's argument to the contrary, the Note was properly obtained and assigned. As the trial court correctly observed, the record demonstrates that, on February 27, 2004, Sunset Mortgage extended credit to Brooks in the amount of $379,200.00 and Brooks signed the Note which reflected this event. The record also reflects that Sunset Mortgage immediately assigned the Note to WAMU. This was accomplished by an allonge which is attached to the Note. The document formalizing Chase's acquisition of WAMU constituted substantial evidence that the Note was among those assets Chase acquired from the FDIC following WAMU's placement in receivership. Therefore, the record demonstrates that Chase is a holder in due course of the Note on the Brooks property, and it had standing in this case to assert such an interest.

There was substantial evidence of record showing that a debt was incurred in 2004; that debt was secured against the Brooks property; and that Chase now properly holds the Note on that debt. The trial court committed no

clear error in so finding, nor did it err in concluding that the Note was sufficient to make Chase a holder in due course of an equitable mortgage. The trial court's decision on these points finds support in Kentucky law.

DeMoisey also argues on appeal that the trial court could not have grounds to dismiss without granting its motion to compel discovery of documents and information relating to Chase's acquisition of WAMU's assets, including the Note in this case. However, we have concluded that the record adequately demonstrated Chase's acquisition of the Note. Accordingly, we agree with the trial court that this issue is moot.

II. Priority of Liens

Finally, we next address whether the trial court erred in holding that Chase's lien was superior to DeMoisey's. DeMoisey argues that its lien is superior because its lien is the only one which was "lawfully recorded." It also argues that Chase's *lis pendens* notice, which it filed a month prior to the recording of DeMoisey's mortgage, is insufficient by itself to provide Chase's lien with priority. While we agree with DeMoisey's latter point, the trial court did not rely exclusively upon Chase's *lis pendens* notice. More importantly, DeMoisey's former point finds opposition in well-established Kentucky law.

In *State Street Bank v. Heck*, 963 S.W.2d 626, 630 (Ky. 1998), Kentucky's Supreme Court unequivocally held that a prior equitable mortgage takes priority over a subsequent lien recorded with actual or inquiry notice of the prior lien. *See also* KRS 382.270 (establishing, more generally, Kentucky's status

as a "race-notice" jurisdiction). This is where Chase's *lis pendens* notice, filed one month before DeMoisey filed his mortgage, becomes vital to the outcome of this case. It is fundamental in the law that a party who takes a lien against a property upon which a *lis pendens* notice has already been filed does so "subject to the results of the litigation" of which the *lis pendens* notices that party. *Strong v. First Nationwide Mortg. Corp.*, 959 S.W.2d 785, 787 (Ky. App. 1998), citing *Cumberland Lumber Co. v. First and Farmers Bank of Somerset, Inc.*, 838 S.W.2d 403, 405 (Ky. App. 1992). The record clearly reflects that DeMoisey filed its mortgage after Chase filed its *lis pendens* notice. Therefore, DeMoisey is a *pendente lite* lienholder and "can have no greater interest in the property at issue" than Chase, which held a prior and lawful lien.

Conclusion

The very nature of an equitable mortgage is that, where certain documents memorializing an otherwise legal and binding transaction are lost or incomplete, the party who provided credit, or who assumes the burden of that credit, does not forfeit its interest. There is no disputing that the Mortgage and its execution were faulty. However, while DeMoisey focuses much of his argument on that self-evident fact, we are tasked with determining what, if any, impact those faults had on Chase's interest and the existence of an equitable mortgage.

To that end, the record reflects that in 2004, Chase's predecessor in interest extended credit to Brooks, thereby obtaining a lien on the subject property; Chase's predecessor in interest held, and eventually assigned, a promissory note

reflecting this fact; and Brooks subsequently made payments on this indebtedness. Therefore, it is indeed "equitable" that Chase's interest in the Brooks property be protected, notwithstanding the imperfect manner in which this transaction began. More importantly, Chase established as a matter of law that, despite faults with the actual mortgage document, it held an equitable mortgage on the Brooks property and that its lien took priority over all others, including DeMoisey's.

Therefore, the April 16, 2015, order of the Fayette Circuit Court is affirmed.

JUDGE STUMBO CONCURS.

JUDGE TAYLOR DISSENTS AND WILL NOT FILE SEPARATE OPINION.

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